Notes from the Trading Desk

November 18, 2019

Ben Carew, CFA
Tandem Investment Advisors

Market Mover & Shakers

Nearly all of the major domestic indices traded higher last week. The Dow, the S&P 500, the Nasdaq, and the Russell Mid Cap all moved higher and closed at all-time highs once more. The only outcasts were the Russell 2000 and the Dow Jones Transportation Average. The Russell 2000 fell 15 bps and remains a little more than 8% off its September 2018 high, and transports remain roughly 6% below their September 2018 high as well. The poor performance of transports and the two month slide in the Baltic Dry Index — which measures the cost of transporting raw materials — are both likely indicative of the still present fear of the global slowdown. Elsewhere, bonds continue to be rather range bound. The 10-year U.S. Treasury has traded between 1.5% and 2.0% since the end of July. Meanwhile, the 2-year has been bouncing between 1.4% and 1.8%. Interestingly enough, there has been a slight up-tick in the spread between Treasuries and junk bonds. In fact, *The Wall Street Journal* reported on Monday that the CLO market has actually stumbled of late. CLO bonds had returned about 10% through June, but have since fallen enough to give investors a 1% return YTD. A continuation of the trend could signal further unrest in the marketplace.

It truly is remarkable how much price changes sentiment. Bank of America Merrill Lynch's fund manager survey was released last week and it reported that cash levels have dropped to their lowest levels in over 6 years. What's more, it was actually the largest drop in cash levels since the 2016 election. CNN's Fear and Greed Index recently reached levels it had not seen in 2 years — surpassing even levels we saw during the blowout top to start 2018. The change in sentiment can also be seen in the recent outperformance of cyclicals and growth. While the S&P 500 is off to a great start this quarter, up 4.83%, its performance pales in comparison to the likes of semiconductors (up ~12% QTD), the tech sector (up ~8% QTD), and NYSE's FANG+ Index (up ~11% QTD). There has been a clear surge into tech so far this quarter.

Despite the recent rush into equities, and more specifically tech stocks, market breadth has not been remarkably strong. Now, I am not one to put too heavy an emphasis on technical formations. However, last week MarketWatch reported the formation of the Hindenburg Omen and the Omaha Titanic Syndrome. The names are unimportant, but the gist of the two indicators is much more important. Essentially, what these indicators tell us is that there have recently been more stocks setting 52 week lows than 52 week highs — an uncommon occurrence with so many indices trading at all-time highs. It means that performance has been confined to a rather narrow group of names that have led the recent rally. Hence the Russell 2000 is still more than 8% of its high set 14 months ago. Prior to the big move Friday, the market had actually become rather muted. In fact, the previous 5 trading sessions prior to Friday saw the Dow move a whopping 110 points — including a day in which the Dow closed completely flat. The 5-day 110 point move created the least volatile period since early 2017.

Speaking of volatility, a Morgan Stanley research team recently put out a note titled "What will Markets Return? 2019 Edition". The piece discussed their team's forecast for heightened volatility and subdued returns moving forward over the next decade. While their call for increased volatility and low returns might seem alarming to some, it is an environment that we have all become increasingly familiar with over the past two years. Since the January 2018 high, the S&P 500 is up 7.6%. That is an annualized return of a little more than 4%, which is well below the long-term average of the index. However, volatility (as measured by standard deviation of monthly returns) since that January 2018 high has been above-average relative to the past 30 years. In other words, we have been in the midst of the environment that Morgan Stanley describes for nearly two years now. If Morgan Stanley is correct in their call for lower returns and increased volatility, then it will likely be more important than ever to limit volatility in one's portfolio. Volatility is the enemy of the retail investor. Too often volatility causes investors to react impulsively and incorrectly. In 2015, Dalbar Inc. published a study in which they found equity investors over the course of the 20 years ending 12/31/2014 underperformed the market by 4.66% annually. They attributed this underperformance to a multitude of reasons surrounding investor psychology and the average investor's tendency to act emotionally. At Tandem, our investment philosophy is predicated on attempting to limit volatility in one's portfolio, which we believe allows one to outperform over complete market cycles. Lastly, by following a discipline that is built upon math and numbers, we believe we are able to better avoid the damage to one's portfolio that may result from emotional decision making.

*Transition Update***

With earnings season now mostly wrapped up — with the exception of retail — we were a little less active this past week than we have been for much for the quarter. However, we did still purchase a few names on the transition level. First, we continued to take advantage of the attractive valuations in J.M. Smucker, Johnson & Johnson, and C.H. Robinson, as we bought all three on the transition level. We also had the opportunity to purchase Fiserv in our Mid Cap transition accounts, as Fiserv appears to have hopefully broken out from their 4-month trading range. We also purchased some Stryker Corp. Stryker seems to have potentially found a bottom around $200 following its recent 10% slide. Lastly, we also purchased some Dollar Tree, eBay, Verisk Analytics, and Yum! Brands. All four stocks have gotten hit over the last few months having dropped 8%, 14%, 14%, and 18%, respectively from their YTD highs.

***The transition update describes activity taken by Tandem on the transition level, not the composite or firm-wide level. The transition update is applicable to new accounts and new money. New accounts and new money are not automatically invested on the first day. Rather, they are transitioned into our strategy over a longer time period that is dependent upon market conditions. This update describes that transition.*

Portfolio News & Notes

Over the previous two weeks we finished our liquidation process in two of our core holdings. Billy touched on the liquidation of CVS in his most recent *Observations*. We also finalized the liquidation of CVET in our Mid Cap strategy. We have continued to build out a position in a new name. The new name will be discussed more in depth once the position is finished being built out.

Walgreens started the week off with a bang as it was announced that KKR had been preparing a proposal to take Walgreens private. The news of KKR's interest had actually caused a slight pop in the stock on November 5th. However, the news was seemingly confirmed last Monday, which caused another quick jump in the stock. Other than that, it was a fairly slow week in terms of news flow. Nike released a statement that they will no longer sell Nike products on Amazon. Elsewhere, Abbott's longtime CEO, Miles White, will be stepping down on March 31st of next year. White has been with the company for 35 years and became CEO in 1999. The board announced that his successor will be Robert Ford, who currently serves as President and COO. Ford joined Abbott in 1996. J.M. Smucker also announced the retirement of CFO Mark Belgya, effective September 1, 2020. SJM also promoted from within, as they promoted Tucker Marshall VP of Finance. Belgya had spent the last 15 of his 35 years with the company as CFO. Tucker has been with the company for nearly 8 years.

Lastly, I would be remiss to not mention the newest addition to our team here at Tandem. Jordan Watson has joined us in the role of Investment Management Associate. Jordan graduated from the College of Charleston in 2018 and has joined us after a year and a half at Cornerstone Wealth Advisory Group. We are excited to have Jordan on board!

	WTD	MTD	QTD	YTD
Dow Jones	1.17%	3.54%	4.04%	20.05%
S&P 500	0.89%	2.73%	4.83%	24.48%
Nasdaq	0.77%	3.00%	6.77%	28.72%
Russell 2000	-0.15%	2.18%	4.80%	18.38%
Comm. Svcs	1.34%	3.38%	6.20%	27.99%
Con Disc	-0.24%	0.18%	0.47%	21.78%
Con Staples	0.85%	0.32%	-0.02%	20.58%
Energy	-1.28%	3.23%	0.75%	3.86%
Financials	-0.26%	3.62%	5.95%	24.58%
Health Care	2.41%	2.85%	7.99%	12.54%
Industrials	0.57%	4.69%	5.72%	27.70%
Info Tech	1.31%	4.24%	8.21%	40.53%
Materials	0.24%	3.73%	3.75%	19.49%
Utilities	1.53%	-2.46%	-3.24%	18.33%
REITs	1.90%	-2.27%	-2.45%	23.42%

Upgrades/Downgrades & Dividends

CHKP — Initiated neutral at Goldman Sachs with a price target of $123 (11/12).

CMCSA — Target revised at HSBC to $52 from $45, the stock remains a buy (11/14).

NKE — Initiated overweight with a price target of $111 at Barclays (11/13).

NKE — Increased their quarterly dividend by 11.4% to $0.245 from $0.22, record date December 2 (11/14).

ROST — Initiated overweight with a price target of $124 at Barclays (11/13).

ROST — Initiated outperform at RBC Capital Markets with a price target of $120 (11/11).

SJM — Downgraded to underperform from neutral at Credit Suisse with the price target cut from $100 to $95 (11/13).

TJX — Initiated sector perform with a price target of $60 at RBC Capital Markets (11/11).

TJX — Initiated overweight with a price target of $66 at Barclays (11/13).

Earnings Calendar

Date	Time	Ticker
11/19	Pre-Market	TJX
11/21	Post-Market	ROST
11/22	Pre-Market	SJM